



Financial Robots as Instruments of Fiduciary Loyalty

Never Stand Still

Law

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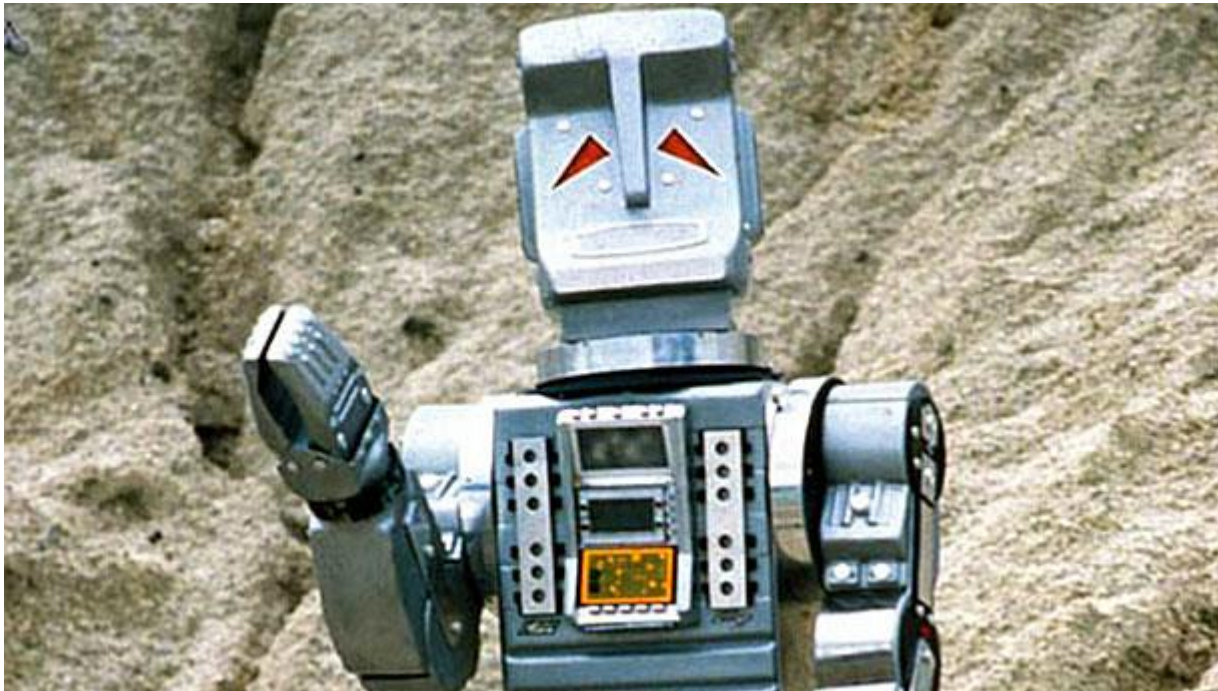
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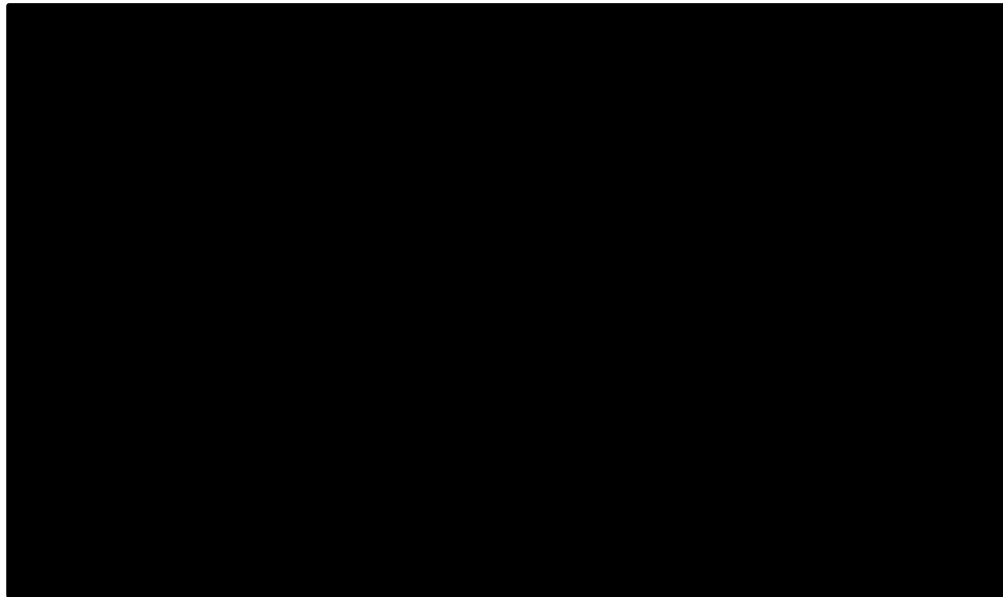
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Financial Robot?



Financial Robot?



Presentation outline

Robo advice

Summary

**Paradigm
course of
dealing**

**Equitable
fiduciary
duties**

**Disclosure &
consent**

**Compliance
& remedies**

**What is robo
advice?
Why is it advice?**

**Summary of
research
question and
findings**

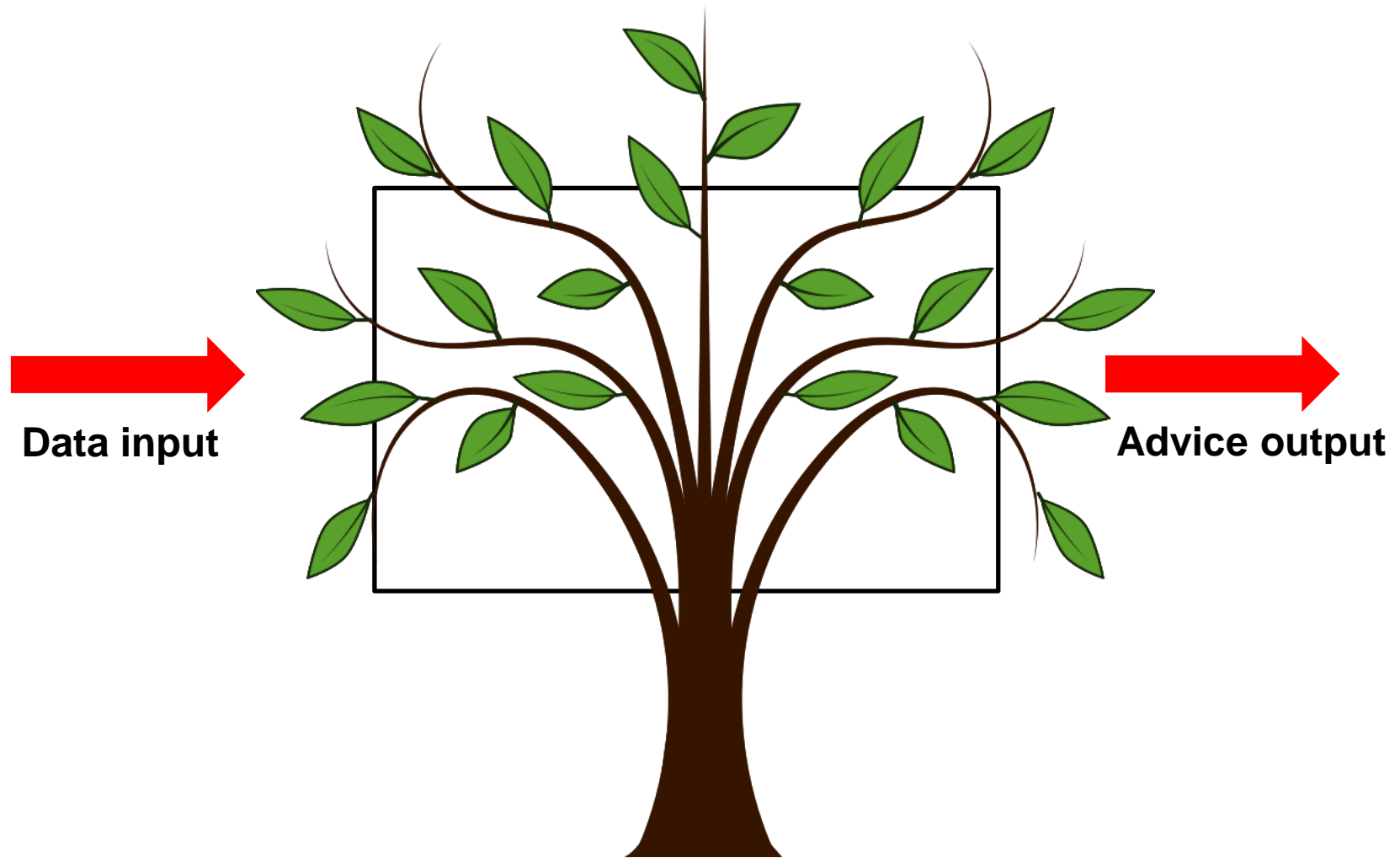
**Substantive
advice / advice
about advice
Robo advice
hypotheticals**

**Existence
Content
Breach**

**Equity's
stringent
standards
Contracting out
not possible**

**Significance?
Parts 7-7.7A of
the Corps Act
compliance
irrelevant
Risk of equity's
remedies &
implications for
AFSL
compliance**

Robo advice?



Summary

1. Robo advisers may be fiduciaries for their clients.
2. Equity's prohibitions against conflicts and potential conflicts of duty and interest, conflicts between multiple duties, and against taking a profit apply.
3. Extrapolating from the paradigm course of dealing given by ASIC (ASIC RG 255, Digital X example) and the requirements of Parts 7.7, 7.7A and 7.9 of the *Corporations Act 2001* (Cth), we argue that it is difficult for the adviser to contract out of fiduciary duties. Further, the fullest of fiduciary disclosure and informed client consent cannot systemically be obtained.
4. Structural drivers towards breach of fiduciary duties, and compliance with Parts 7.7, 7.7A and 7.9 of the *Corporations Act* does not systemically ensure discharge of equitable fiduciary duties.
5. Potential equitable remedies: account of profits, equitable compensation & rescission.
6. Fiduciary breach may result in failure to comply with licensee's obligation to 'do all things necessary to ensure that the financial services ... are provided efficiently, honestly and fairly'. A further risk is that a director of the company that is the advice provider or holder of the AFSL under which the advice is provided may face personal liability for breach of directors' duties (see *ASIC v Cassimatis* [2016] FCA 1023, [833] (Edelman J)).

Paradigm course of dealing



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Robo advice hypothetical

Acknowledgment & Agreement Upon Entry

Client enters robo advice platform via a window that requires the client to acknowledge and agree to the terms and conditions, receipt of the FSG and disclaimers. This window might also contain links to the FSG and Terms and Conditions, allowing the client to view these documents prior to entry into the robo advice platform.

I agree / Click here to get started / Start

By clicking on the link above you acknowledge that you have read and understood, and agree to the Terms and Conditions and Financial Services Guide, available here.

Robo advice hypothetical

Gateway questions

Client will be asked a series of questions to ascertain the client's financial objectives, personal circumstances, and risk tolerance relevant to the type of advice sought.

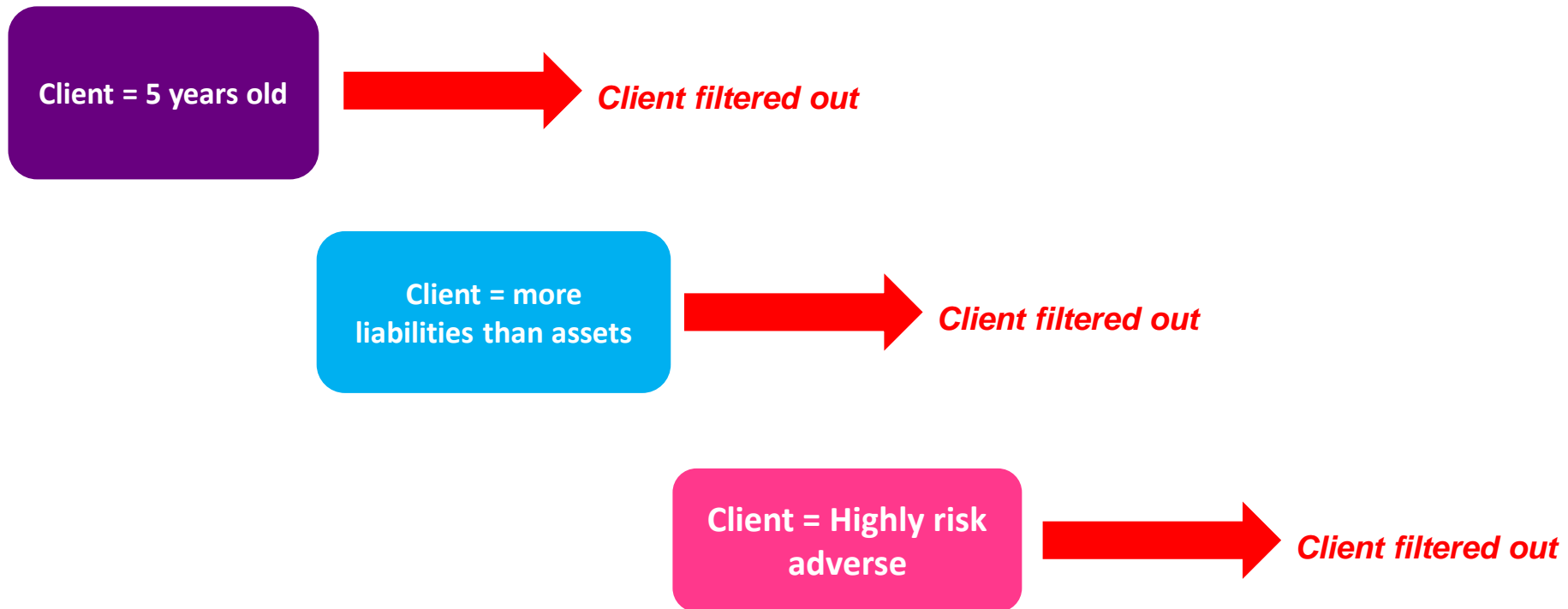
Age?
Income?
Assets?
Liabilities?
Income?
Expenditure?

Client asked to
identify life
objectives, such as:
Security in
retirement
Pay for children's'
education
Own home
Nest Egg

Investment
time frame
Risk profile /
tolerance

Robo advice hypothetical - Allocation to decision outcome #1: Filtered out

At any time the client might be filtered out of the platform if deemed unsuitable to receive robo advice. This outcome is also advice.



Allocation to decision outcome #2: Client offered substantive advice on selected topic area

Statement of Advice

- Advice summary
- Scope of advice
- Client information on which advice is based
- Detailed advice
 - Investment strategy, recommendation to buy or sell particular financial products or class of products
 - Explanation for recommendation – benefits
 - Important information / risks
- Fees and costs
- Client acknowledgements and permissions

Robo advice hypothetical

Advice implementation and execution

Client directed to platform for implementation and execution of advice.

Platform might be contained within robo advice where adviser also offers execution and management services etc, or client directed to another platform hosted by related services provider.

[Click here to invest](#)

[Authority to proceed]

By clicking here you acknowledge that the products listed in the SOA are to be acquired by Robo on your behalf according to the agreement [set out here](#)

OR

[Click here to invest](#)

[client directed to another platform hosted by related services provider]

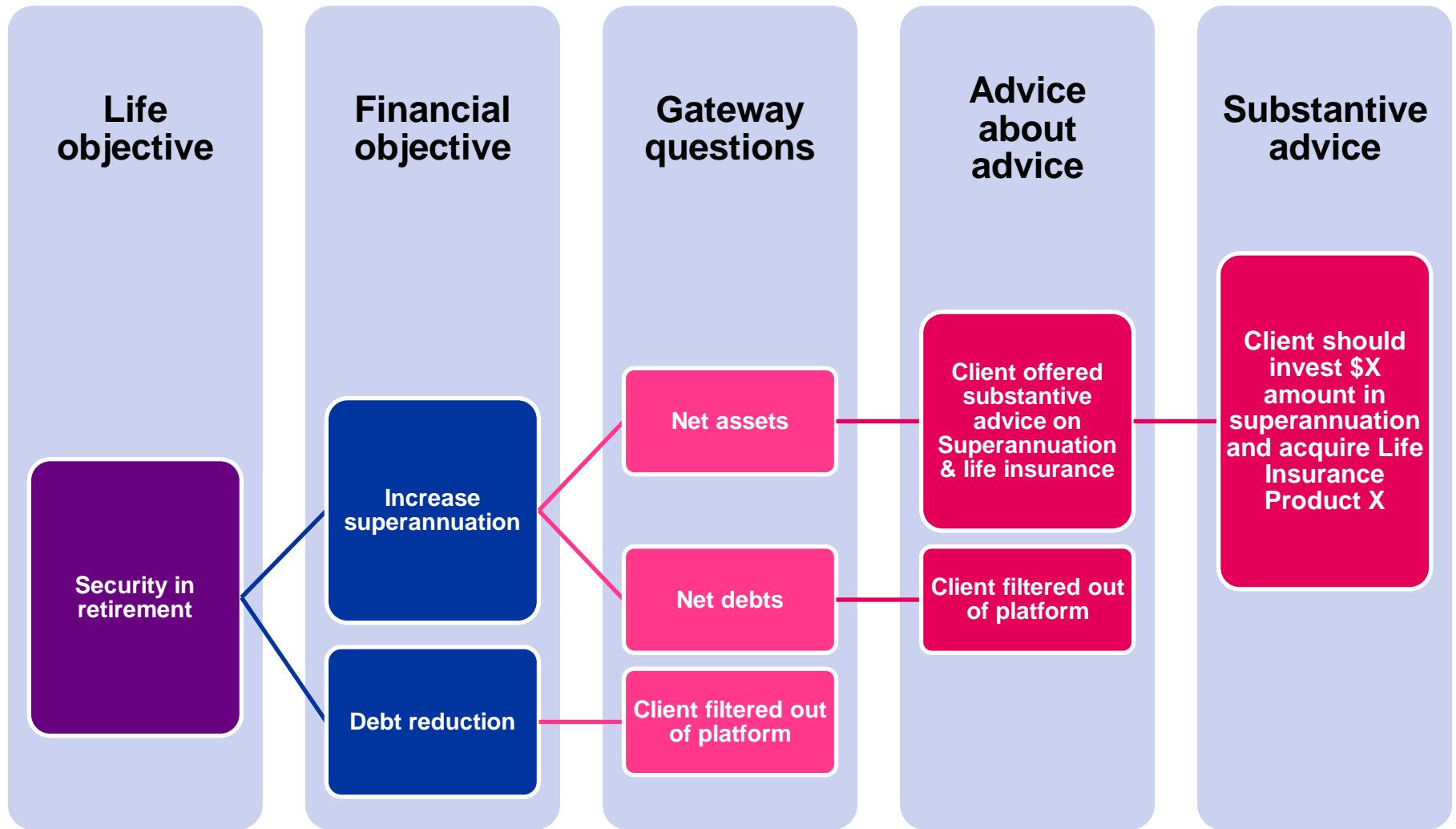
Robo advice encompasses two types of advice

Substantive advice is advice capable of implementation by the client concerning actual investments or investment strategies, and includes for example, financial product advice.

Advice about advice is a conceptually preliminary recommendation by the adviser. It may encompass, for example, the threshold question of whether or not the client should receive substantive financial advice. Alternatively, advice about advice may relate to the selection of the topic areas of advice on which the client will receive substantive advice. Advice about advice is conceptually preliminary, but depending on the course of dealing, may or may not occur prior in time to the substantive advice.



The Decision Tree



Financial robo advisers as fiduciaries

- Financial adviser and client relationship?
- Fiduciary relationship on the facts – a financial adviser will constitute itself a fiduciary where the financial adviser holds itself out as having specialised expertise and undertakes to give advice to a client who relies upon the expertise of the adviser and the adviser’s undertaking to act in the client’s interest.
- A fiduciary relationship potentially arises from all three paradigm courses of dealing: life objectives filter, financial objectives filter; single topic of advice platform.

Financial Advisers as Fiduciaries

“whenever a stockbroker or other person who holds himself out as having expertise in advising on investments is approached for advice on investments and undertakes to give it, in giving that advice the adviser stands in a fiduciary relationship to the person whom he advises. The adviser cannot assume a position where his self-interest might conflict with the honest and impartial giving of advice”

385, (Brennan J)

Daly v Sydney Stock Exchange Ltd [1986] HCA 25; (1986) 160 CLR 371

Financial Advisers as Fiduciaries

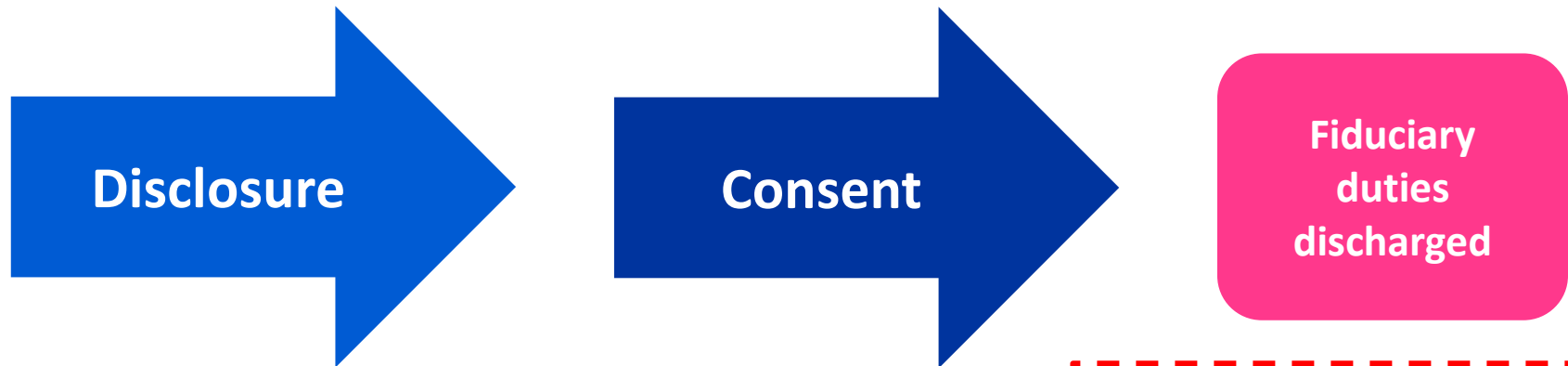
Mason J's *essence* of fiduciary relationships, giving a list which “...form the illustrations which the judicial decisions provide...” (96).

“The critical feature of these relationships is that the fiduciary undertakes or agrees to act for or on behalf of or in the interests of another person in the exercise of a power or discretion which will affect the interests of that other person in a legal or practical sense.”

USSC v Hospital Products (1984) 156 CLR 41, 96-97 (Mason J).

Example	Scope of fiduciary duty	Breach	Disclosure and consent
Life objectives filter	<p>1. Translation of life objective into financial objective and particularising into suitable topic areas for advice, or filter out (<i>advice about advice</i>)</p> <p>2. Content of substantive investment advice (<i>substantive advice</i>)</p>	<p>Presentation of closed set of topic area(s) for self-interested reasons, limited by licence</p> <p>Decision whether to advise or not for self-interested reasons</p>	<p>Client acknowledgements – potentially insufficient as disclosure cannot be calibrated</p> <p>FSG – may contain disclosures relevant to conflict, eg commission and fees, but only generic. Further problem may be passive or no consent. Can't meet the sophistication and intelligence of client</p>
Financial objectives filter	<p>3. Translation of financial objective into suitable topic areas for advice, or filter out (<i>advice about advice</i>)</p> <p>4. Content of substantive investment advice (<i>substantive advice</i>)</p>	<p>Duty / duty breach</p>	<p>SOA – <i>may</i> contain disclosures relevant to conflict, eg commission and fees, but will chronologically be too late. Further problem as client may be passive and disclosure can't meet the sophistication and intelligence of client</p> <p>Clients filtered out – no SOA</p>
Single topic of advice platform	<p>5. Client permitted to proceed to advice outcome or filter out (<i>advice about advice</i>)</p> <p>6. Content of substantive investment advice (<i>substantive advice</i>)</p>	<p>Decision whether to advise or not for self-interested reasons</p> <p>Duty / duty breach</p>	<p>Duty/ duty – decision tree not designed to capture relevant information to reveal any conflict or potential conflict. Disclosure therefore systemically difficult</p>

Disclosure & consent



Full disclosure of the nature and extent of the breach

- Eg must disclose: adviser's personal interest in steering a client towards one topic area of advice over another.
- The level and degree of disclosure depends upon the client's sophistication.
- Robot cannot tell if client is 'shrewd and astute' or 'babe... in the woods' (*Farah v Say-Dee*, [108]).

Client consent

- Question of fact in all the circumstances & no precise formula.
- Client must consent to the adviser's conflict.
- Passive acceptance following disclosure may be insufficient for consent. Did the client turn their mind to nature and extent of the conflict and whether to provide consent?

Statutory disclosures – do not discharge

- **FSG** – may or may not be timely, but is not sufficiently detailed or calibrated to provide the basis for informed client consent.
- **SOA** – provides for fuller disclosure, but may not be calibrated and comes too late in the relationship adequately to disclose, consent / ratify any earlier breach.
- **PDS** – too little too late.

Risk of fiduciary breach remains

- Assuming this pattern of interaction, there is a risk of a fiduciary relationship arising, albeit narrow in scope, between adviser and client. We argue this arises very early in any interaction between adviser and client.
- Meeting the requirements of the statute will not (incidentally) discharge the requirements of equitable obligation.
- This has implications for conduct and compliance systems calibrated particularly to the *Corporations Act* without also considering the separate risk of fiduciary breach.
- Risk of equitable remedies:
 - Account of profits
 - Equitable compensation
 - Rescission.
- Breach of fiduciary duty may result in licensee's failure to comply with obligation to 'do all things necessary to ensure that the financial services ... are provided efficiently, honestly and fairly'.
- A further risk is that a director of the company that is the advice provider or holder of the AFSL under which the advice is provided may face personal liability for breach of directors' duties (see *ASIC v Cassimatis* [2016] FCA 1023, [833] (Edelman J)).

Questions?

See also:

- S Degeling and J Hudson, 'Financial Robots as Instruments of Fiduciary Loyalty' (2018) 40 *Sydney Law Review* (in press).
- S Degeling and J Hudson, 'Equitable money remedies against advisers who give "advice about advice"' (2015) 33 *Company and Securities Law Journal* 166-175.
- S Degeling and J Hudson, 'Fiduciary Obligations, Financial Advisers and FOFA' (2014) 32 *Company and Securities Law Journal* 527-539.

